THE DFI UPDATE

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RECENT CONVERSIONS

On April 5, 2001, the Members of the Indiana Department of Financial Institutions approved the conversion of Old Kent Bank, N. A., Jonesville, Michigan into an Indiana chartered commercial bank. The newly converted institution will be known as Fifth Third Bank, Indiana and will be headquartered at 251 N. Illinois Street, Indianapolis, Indiana. (Yes, this is the same headquarters of the previous Fifth Third Bank, Indiana prior to its merger into Civitas Bank, St. Joseph, Michigan in March 2000.) After the conversion, Fifth Third Bank, Indiana headquartered in St. Joseph, Michigan will be merged into the new Indiana chartered institution. The restructuring also includes the purchase of certain Indiana branches from Old Kent Bank, Grand Rapids, Michigan as well as the sale of some branches to Old Kent Bank. The resulting bank is projected to have total assets of approximately $8 billion and 147 branches extending throughout Indiana, southern Illinois and Kentucky. Michael Alley will be the President and CEO of the new bank. The transactions were approved by the Federal Reserve Bank on May 14, 2001.

The Members of the Indiana Department of Financial Institutions also approved the conversion of Ameriana Bank and Trust of Indiana, New Castle, Indiana, from a federal stock savings bank to a state chartered stock savings bank. Upon conversion the savings bank will be known as Ameriana Bank and Trust, SB. As of December 31, 2000, Ameriana Bank and Trust of Indiana had total assets of $557 million. Harry Bailey will continue to be President and CEO of the savings bank. Additionally, there will be no changes in the directors, officers, or operating personnel of the savings bank, due to the conversion. The conversion is expected to be consummated prior to June 30, 2001.

Gina Williams and Kirk Schreiber

FINANCIAL RESULTS DIVISION OF BANKS AND TRUST COMPANIES

From January 1, 2000, to December 31, 2000, the number of state-chartered commercial banks, stock and mutual savings banks, and active industrial authorities declined in number from 131 to 128. During the same period total supervised assets increased from $25.6 billion to $26.1 billion. As of December 31, 2000, state-chartered commercial banks represented 31% of total Indiana bank assets (state and national). In contrast, state-chartered commercial banks represented 81% of the total number of such banks in the state of Indiana. As of December 31, 2000, there were 31 national and 128 state-chartered banks in Indiana.

During the calendar year of 2000, three new state-chartered commercial banks officially opened for business: United Commerce Bank, Bloomington, Goshen Community Bank, Goshen and Lafayette Community Bank, Lafayette. Four state bank charters were eliminated through mergers with other state, national or federal savings banks.

The calendar year of 2000 continues to show the strong trends of Indiana state chartered financial institutions in condition and performance. Net income as a percentage of average assets decreased slightly from 1.19% as of December 31, 1999 to 1.17% as of December 31, 2000. The aggregate loan and lease loss allowance decreased from l.35% of total loans in 1999 to 1.26% of total loans as of December 31, 2000, due to loan growth outpacing provision expense. Net charge offs for 2000 increased to 0.17% of total loans compared to 0.13% for 1999. Equity capital remains at an adequate level as equity capital increased from 9.13% to 9.63% of total assets from year-end 1999, to year-end 2000.

The trend analysis utilized the following consolidated balance sheet, consolidated income statement and ratio analysis for all state chartered commercial banks, savings banks, active industrial authorities and national commercial banks. Information to compile these schedules was obtained through the Federal Deposit Insurance Corporation's Database.

Kirk Schreiber

FINANCIALS CONTINUED ON PAGE 4

ACCOUNT DESCRIPTIONS ***(IN MILLIONS OF $)***	State 12/31/00	National 12/31/00	State 12/31/99	National 12/31/99	State 12/31/98	National 12/31/98
Number of Banks	128	31	131	33	138	38
Income Statement						
Total Interest Income	1,901	3,958	1,759	2,739	1,780	3,121
Total Interest Expense	949	2,063	799	1,201	850	1,470
Net Interest Income	952	1,895	960	1,538	930	1,651
Total Non Interest Income	375	1,217	237	1,532	233	1,052
Loan Provisions	55	186	46	120	55	141
Total Non Interest Expense	816	2,220	689	1,805	661	1,632
Net Income	285	413	284	730	298	632
Ratio Analysis						
Net Income to Average Assets	1.17%	0.80%	1.19%	1.85%	1.26%	1.58%
Net Income to Total Equity	11.33%	7.90%	12.17%	19.45%	12.81%	14.90%
Net Interest Income To Average Assets	3.91%	3.65%	4.02%	3.89%	3.93%	4.12%
Total Loans to Average Assets	74.54%	77.87%	73.76%	64.67%	71.70%	85.60%
Total Loans to Total Deposits	88.11%	116.09%	88.95%	97.15%	82.84%	98.24%
Loan Loss Provisions to Total Loans	0.30%	0.46%	0.26%	0.47%	0.32%	0.41%
Loan Loss Reserves to Total Loans	1.26%	1.39%	1.35%	1.65%	1.37%	1.39%
Net Charge-Offs to Total Loans	0.17%	0.43%	0.13%	0.44%	0.21%	0.38%
Total Equity Capital to Total Assets	9.63%	8.78%	9.13%	9.29%	9.16%	8.68%
Total Equity Capital and Reserves to Total Assets and Reserves	10.41%	9.63%	9.96%	10.23%	9.98%	9.56%

ACCOUNT DESCRIPTIONS *(IN MILLIONS OF $)*	State 12/31/00	National 12/31/00	State 12/31/99	National 12/31/99	State 12/31/98	National 12/31/98
Number of Banks	128	31	131	33	138	38
Balance Sheet						
Trading Accounts	146	446	58	2	20	8
Interest Bearing Balances	146	272	130	250	168	495
Fed Funds Sold/Repurchase Agreements	544	1,027	409	719	737	1,512
Total Securities	5,877	11,695	6,036	9,145	5,572	6,422
Total Loans	18,129	40,408	17,613	25,562	16,931	34,263
Total Earning Assets	23,778	51,719	23,412	34,284	23,428	42,700
Total Assets	26,120	59,511	25,575	40,391	25,407	48,881
Average Assets	24,322	51,893	23,880	39,527	23,614	40,028
Total Deposits	20,575	34,807	19,802	26,313	20,437	34,876
Total Liabilities	23,605	53,826	23,241	36,115	23,079	44,638
Total Equity Capital	2,515	5,227	2,334	3,753	2,327	4,243
Loan Valuation Reserves	228	560	237	423	232	476
Total Equity Capital & Reserves	2,743	5,787	2,571	4,176	2,569	4,719
Total Other Real Estate	14	33	9	22	9	19
Total Charge-Offs	42	225	39	180	52	190
Total Recoveries	12	52	16	68	17	60
Net Charge-Offs	30	173	23	112	35	130

INDUSTRY CONSOLIDATION AND NEW FINANCIAL INSTITUTIONS

As a part of the Department's ongoing monitoring process, the staff of the Department looks to pending or anticipated mergers and acquisitions. Currently, the Department has sixteen banks that are being tracked as institutions that may be merged out of existence. These sixteen institutions have total assets of approximately $2.4 billion and are controlled by seven bank holding companies. During the calendar year 2000, six commercial banks merged out of existence. The assets removed from state regulation due to these six institutions merging totaled nearly $2.7 billion.

In contrast, the consolidation has slowly drawn the institutions away from local control into more regional management, and therefore, has heightened interest by community leaders in forming new banks. A financial institution may not be organized until the requirements established in IC 28-11-5 have been satisfied. Since December 31, 1999, three newly formed commercial banks opened for business.

The Department approved United Commerce Bank on October 14, 1999. This institution officially opened on January 31, 2000. The institution is located in Bloomington, Monroe County, Indiana. As of December 31, 2000, United Commerce Bank had $35.8 million in total assets. On May 11, 2000, the Department approved Lafayette Community Bank, Lafayette, Tippecanoe County, Indiana. Lafayette Community Bank officially opened on October 30, 2000. As of December 31, 2000, Lafayette Community Bank had $9.8 million in total assets. The Department also approved Goshen Community Bank, Goshen, Elkhart County, Indiana on August 10, 2000. This institution officially opened on September 29, 2000. As of December 31, 2000, Goshen Community Bank had $8.3 million in total assets.

Additionally, the Department has approved two institutions intending to convert to Indiana state charter financial institutions. On April 5, 2001, the Members of the Department approved the conversion of Old Kent Bank, N.A., Jonesville, Michigan into an Indiana chartered commercial bank. The newly converted institution will be known as Fifth Third Bank, Indiana and will be headquartered at 251 N. Illinois Street, Indianapolis, Indiana. On the same day, the Members also approved the conversion of Ameriana Bank and Trust of Indiana, New Castle, Indiana, from a federal stock savings bank to a state chartered stock savings bank. Upon conversion the savings bank will be known as Ameriana Bank and Trust, SB.

Kirk Schreiber

EXAMINERS TO MONITOR ARTICLE 9 PREPAREDNESS

The National Conference of Commissioners on Uniform State Law and the American Law Institute have drafted major revisions to Article 9 of the Uniform Commercial Code (UCC). Article 9 governs transactions involving the granting of credit secured by personal property and the sale of accounts and chattel paper. The revised Article 9, however, does not become law within a particular state until it has been adopted by the state legislature. In Indiana, the provisions of revised Article 9 are codified at IC 26-1-9.1 with an effective date of July 1, 2001. The revised provisions codified in Indiana can be found at www.state.in.us/legislature/ic/code.

The revised Article 9 contains a number of new or revised rules for secured transactions that will affect a financial institution's procedures, systems, documentation, and enforceability of security interests. All financial institutions and their legal counsel should carefully consider the changes in state law in order to ensure the attachment and perfection of their existing and future security interests.

To properly prepare for the revised Article 9, all financial institutions are expected to:

- Become fully aware of the changes to the Indiana Code to implement Article 9 and determine the effect the changes will have on the institution;

- Determine the need for revised policies, procedures, systems and documentation and implement the revisions as necessary;

- Review secured transactions entered into under existing Article 9 to ensure that existing rights are protected under the revised provisions and make changes as necessary;

- Provide adequate training to ensure the staff understands the revisions to Article 9 and can effectively implement revisions to existing policies and procedures.

DFI Central Point of Contact (CPC) examiners will be contacting all supervised institutions engaged in secured lending to determine their plans for compliance with the revised Article 9 and Indiana Code provisions. The initial contact will be made by the CPC sometime prior to the July 1, 2001 effective date. Examiners will assess the adequacy and appropriateness of the institution's plans. Continual monitoring and assessment will also occur following the effective date through remote contact and on site examination activities.

Randy Rowe

TRUST PREFERRED SECURITIES

At the January 11, 2001, Member's meeting, the Members of the Department of Financial Institutions adopted a policy to clarify that Trust Preferred Securities (TPS) are allowable investments pursuant to IC 28-1-11-4(a) and IC 28-6.1-10-6(a).

TPS are hybrid instruments. They possess many characteristics typically associated with debt obligations, even though they are denominated as trust preferred securities. The basic structure of TPS are as follows: A corporate issuer organizes a business trust ("Issuer Trust"), usually under the Delaware Business Trust Act. The Issuer Trust issues two classes of securities: (1) common securities, all of which are purchased and held by the corporate issuer; and (2) trust preferred securities, which are sold to investors. The common and trust preferred securities issued by the Issuer Trust represent undivided beneficial interests in the assets of the Issuer Trust. The Issuer Trust's only assets are junior subordinated deferrable interest debentures of the corporate issuer, which are purchased by the Issuer Trust with the proceeds from the sale of the common and trust preferred securities.

The distributions the holders of the TPS receive from the Issuer Trust consist of the interest the corporate issuer pays on the debentures. The distribution rate on the TPS is identical to the rate of interest paid on the underlying debentures. The corporate issuer executes a guarantee of the obligations of the Issuer Trust to pay distributions on the TPS in addition to an agreement to indemnify third parties for other expenses and liabilities incurred by the Issuer Trust. The guarantee provides that if there are not funds to pay the holders of the TPS, the holders can sue the corporate issuer directly to enforce payment. An investment in TPS is functionally equivalent to an investment in the underlying debentures**.**

TPS have characteristics typically associated with debt obligations, such as corporate bonds and municipal revenue bonds.

1) Holders of TPS do not share in any appreciation in the value of the Issuer Trust and are protected from changes in the value of the principal, except for credit risk.

2) Holders of TPS have no voting rights in the management of the ordinary course of business of the Issuer Trust.

3) Holders of TPS may only vote in limited circumstances on issues relating only to the modification of the TPS and the ex ercise of the rights of the Issuer Trust as holder of the debentures and the guaran tee.

4) The distributions on the TPS resemble periodic interest payments on debt.

There are some unique risks associated with TPS that are not typically associated with debt obligations. One unique feature is a deferral option that allows the corporate issuer to defer the interest payments on the subordinated debentures without being in default and as a result the distributions on the preferred securities would be deferred. Some deferral options are permitted for up to 5 years. In addition, TPS can be written to allow the Issuer Trust the ability to extend the maturity of the TPS for up to an additional 20 years without the approval of the TPS holders.

CONTINUED

In 1997, the Office of the Comptroller of the Currency (OCC) considered whether TPS were allowable investments for national banks. In its Interpretative Letter no. 777, the OCC cites several authorities that analyzed TPS and found them to have many substantive features of debt instruments. As such, TPS were found to be eligible investments for national banks as Type III securities, provided they meet the applicable rating and marketability requirements of 12 C. F.R. Part 1.

The FDIC addressed the issue of nonmember banks' ability to invest in TPS in Financial Institutions Letter 16-99. The FDIC determined that Section 24 and Part 362 do not restrict an insured state bank's authority under state law to invest in TPS, provided they meet the investment quality and marketability requirements applicable to national bank's investment in them.

The Office of Thrift Supervision (OTS) issued Thrift Bulletin 73 for guidance to savings associations that wanted to invest in TPS. Due to the lack of data on the performance of TPS over time and the other risks associated with TPS, the OTS placed the following additional limitations and requirements on a savings association's purchase of TPS:

An aggregate investment limit in TPS and securities with similar attributes to 15 percent of total capital;

Prohibition of entering into a formal or informal reciprocal agreement or understanding with another issuer or broker to purchase the securities of another issuer;

Prohibited the investment in a security whose maturity can be unilaterally extended by the issuer beyond 30 years; and

Permitted the purchase of TPS only through a public offering due to liquidity concerns.

The trust preferred securities policy approved by the Members of the Department does not place any additional restrictions on the purchase of TPS other than what are already in place by statute. Examiners will check for compliance with applicable federal guidelines and restrictions. As with any investment decision, the bank must have a full understanding of the risks of the investment and the ability to manage these risks.

It has also come to the Department's attention that some of the newer issues of TPS provide that the TPS are convertible into the common stock of the issuer corporation at some future point in time. The trust preferred securities policy does not give authority to invest in these types of TPS unless it can be determined it would be an allowable investment pursuant to the federal statutes.

Gina Williams

POLICY CONCERNING TRUST PREFERRED SECURITIES

After review and consideration of the information presented at the January 11, 2001, meeting of the Members of the Indiana Department of Financial Institutions, the Members hereby establish the following policy regarding Trust Preferred Securities:

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1) Trust Preferred Securities are considered allowable investment securities subject to the limitations and restrictions pursuant to IC 28-1-11-4 and therefore an allowable investment security for state chartered banks and trust companies.

1) Trust Preferred Securities are considered allowable investment securities subject to the limitations and restrictions pursuant to IC 28-6.1-10 and therefore an allowable investment security for state chartered savings banks.

The Members of the Indiana Department of the Indiana Department of Financial Institutions formally adopted this policy on January 11, 2001.

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Norman Lowery, Chairman

BANK OWNED LIFE INSURANCE

Bank owned life insurance includes all life insurance which a bank purchases or owns or has a beneficial interest in. Life insurance can serve many necessary and useful business purposes. However, life insurance products are complicated and not without risk.

The legal authority for commercial banks and savings associations to purchase life insurance is found at IC 28-1-5-2 (b) (7). Similar authority for savings banks is located at IC 28-6.1-4-1 and IC 28-6.1-4-2. These provisions of the statutes authorize the purchase of life insurance on the life or lives of "designated officers". The statute does not provide authority to purchase life insurance on the life or lives of employees. Title 27 also requires that the bank must obtain the consent of the insured in order to have an "insurable interest". The Department expects compliance with the guidelines contained in OCC Bulletin 2000-23 when state chartered financial institutions purchase life insurance. OCC Bulletin 2000-23 replaces the previous guidelines contained in Bulletin 96-51 dated September 20, 1996. Bulletin 96-51 has been rescinded by the OCC.

Various types of insurance encompassed by the statutory authority would include key-person insurance, insurance on borrowers, insurance purchased in connection with employee compensation and benefit plans, and insurance taken as security for loans. The purchase of life insurance must address a legitimate need of the bank for the insurance. Life insurance may not be purchased to generate funds for the bank's normal operating expenses, for speculation, or for the primary purpose of providing estate planning benefits for insiders unless it is part of a reasonable compensation package. Life insurance purchases must be held consistent with safe and sound banking practices.

The purchase of permanent life insurance subjects the policyholder to several risks. The cash surrender value of most insurance products is subject to credit risk. The cash surrender value is usually a long term, unsecured, non-amortizing obligation of the insurance company. The cash surrender value also subjects the holder to transaction, interest rate, liquidity, compliance, and price risk.

The safe and sound use of bank-owned life insurance depends on effective senior management and board oversight. Regardless of the bank's financial capacity and risk profile, the board must understand the role bank-owned life insurance plays in the overall business strategies of the bank.

Pre-purchase analysis of life insurance products should consider the following standards:

- *Determination of the need for insurance*
- *Quantification of the amount of insurance needed*
- *Selection of Vendor*
- *Selection of Carrier*
- *Review of the characteristics of available insurance products*
- *Analysis of the benefits of the purchase being considered*
- *Determining the reasonableness of any additional compensation*
- *Analysis of the associated risks and ability to monitor and respond to them*
- *Evaluation of alternatives*
- *Documentation of the decision*

Internal quantitative guidelines should be established consistent with prudent risk management practices. These guidelines should generally limit the aggregate CSV of policies from any one insurance company and the aggregate CSV of policies from all insurance companies. Among other things, the bank should consider the legal lending limit (15% of total capital) and the concentration of credit limitations (25% of total capital) when establishing the respective limits. "Separate Account" products have been offered to encourage banks to exceed the limitation to one insurance company. The "separate account" product presents many issues from a safety and soundness and regulatory perspective.

Department representatives are available to discuss any aspects of bank owned life insurance.

Randy Rowe

<u>HOUSE BILL 1705</u>
<u>And</u>
<u>SENATE BILL 345</u>

Governor O'Bannon signed House Bill 1705 and Senate Bill 345 on May 1, 2001. The two bills are identical and were drafted by the staff of the department. The legislation will become effective July 1, 2001.

There are three significant amendments in the bills that effect banks. A new chapter, 28-1-21.10, was added to provide for the conversion of an out-of-state financial institution with branches in Indiana to convert to an Indiana chartered commercial bank. The chapter describes the procedures and requirements for effecting a charter conversion. Present law provides this opportunity to only national banks.

Another new chapter, 28-13-17, was added to accommodate the passage at federal level of the Gramm-Leach-Bliley Act of 1999 signed into law by President Clinton on November 12, 1999 ("GLBA"). The GLBA authorizes national banks to conduct expanded financial activities through financial subsidiaries. Chapter 17 gives the same authority to state chartered financial institutions after obtaining the department's approval.

A new section, 8.5, was added to 28-13-14. This section elaborates on the approval process and requirements that are required for a corporation to do a reverse stock split. Reverse stock splits are becoming more common as financial institutions elect to become a sub-s corporation. The new section provides for dissenters' rights for the minority shareholders in the same way they would be able in a merger transaction.

Other changes allow banks, trust companies, and savings banks to act as agent or broker for insurance companies in other states, addresses foreign corporation filing requirements, requires uninsured financial institutions and corporate fiduciaries to notify the department of the commission of a crime, updates the reference to federal statutes and regulations, and removes the prohibition of a person, firm, limited liability company, or corporation from using the word "trust" as part of its name. The changes do not remove the prohibition on holding ones self out as a "trust" other than a bank, or trust company or corporate fiduciary organized under Title 28 or under the laws of the United States.

House Bill 1705 and Senate Bill 345 also include the legislative changes drafted by the credit union and consumer credit divisions of the department.

Gina Williams

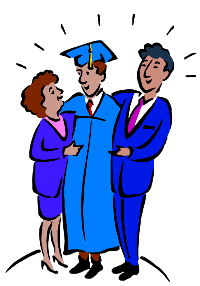
EMPLOYEE SPOTLIGHT

Congratulations to Examiner Scott Imbus and his wife, Melissa on the birth of their son, Jacob Thomas Imbus. Jacob was born on May 6, 2001, and weighed 6 lbs, 14 ounces and is 19 inches long. Jacob was born at St. Vincent's Hospital.

Congratulations to Examiner Steve Wachter and his wife Stephanie on the birth of their daughter, Emily Karen Wachter. Emily was born at St. Vincent's Hospital on February 1, 2001, at 1:04 a.m. She was 6 lbs, 14 ounces, and 20 inches long. Here is a picture of Emily:

Congratulations to Examiner Chad Kozuch and his wife, Stephanie on the birth of their son, Kyler Nicholas Kozuch. Kyler was born on January 25, 2001, at Home Hospital in Lafayette. He was 8lbs 7oz and was 20 3/4 inches long. Here is a picture of Kyler:

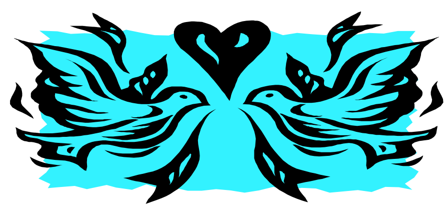
Bank Secretary, Barbara Cole, and her husband, John are pleased to announce that their son, John II graduates in June. John II is the youngest of three children. After graduation, Barb and John plan on traveling to enjoy racing events. Here is a picture of John II:

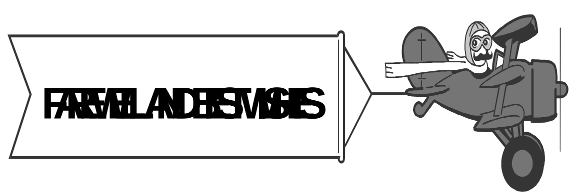


Congratulations John!
D F I would like to wish you a bright and happy future!

Congratulations to Examiner Bruce Allen. Bruce was promoted to FIE II on March 26, 2001.

Congratulations to Examiner Tom Fite and his wife, LeeAnn. They were married on September 30, 2000. Tom and LeeAnn honeymooned at the Aventura Palace in Puerto Rico, Mexico where they enjoyed lots of sun, snorkeling, great food, and the most beautiful surroundings.





Congratulations to Donetta Cooke, Secretary, who retired in February, 2001 after fifteen years with the department. Not only did she retire, but she also married a life-long friend and moved to Pendleton, Indiana.

Congratulations to District 2 Work Leader, Consumer Credit Division, Edward Lay, Jr., who retired on March 30, 2001. Mr. Lay began his career with the department on February 5, 1979. During those 22 years, Ed has gone about the job of being a consumer credit compliance examiner in such a manner as to warrant the respect of his peers and those persons representing the companies he has examined.

WANTED:

YOUR IDEAS

YOUR SUGGESTIONS

YOUR OBSERVATIONS

We are always striving to improve this newsletter, and listening to our readers' suggestions is one way to accomplish this task. Please, if you have any comments or suggestions, feel free to contact Jim Cooper or Tracy Baker at the addresses or numbers below. We are proud of our state banking system and the people who strive to make it work!

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